

Before the
House Committee on Small Business

Business Activity Tax
and Its Impact on Small Businesses

February 14, 2008

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On behalf of the Consumer Electronics Association (CEA), I appreciate the opportunity to appear before you today to highlight a critical issue impacting American small businesses.

By way of background, CEA is the premiere U.S. trade association that represents the \$161 billion consumer electronics industry. We are also the owners and producers of America's largest annual tradeshow, the International CES, held every January in Las Vegas Nevada.

Our more than 2,200 members are involved in the design, development, manufacturing, distribution and integration of audio, video, in-vehicle electronics, wireless and landline communication, information technology, home networking, multimedia and accessory products, as well as related services that are sold through consumer channels. CEA's members include virtually all of America's top technology companies as well as many of the leading retailers.

Approximately eighty percent of our members are small businesses. In fact, our small business members are located in each state represented on this Committee. At the 2008 International CES, almost 1,000 small businesses exhibited; confirming that true American entrepreneurship is alive and well.

Small businesses are the life blood of the United States economy. Given our recent economic uncertainty, it is more important than ever that our legal environment allows small business to thrive. To do so, they need to be subject to consistent regulatory treatment, and fair

and predictable taxation. Unfortunately, our small businesses are now being threatened with onerous and inappropriate taxation by the states. Congress needs to act quickly to stop this alarming trend.

Specifically, an increasing number of states are using “economic nexus” theories to levy income and franchise taxes against out of state companies that have customers but no physical presence in the taxing state. These taxes chill investment and violate the U.S. constitution by unduly burdening the free flow of interstate commerce.

The problem is growing. As of today, a dozen states have developed a statute or regulation that establishes an economic nexus without a physical presence. Several others have made a similar decision at the administrative or judicial levels.

The problems engendered by this growing “crazy quilt” of state levies are obvious. Small businesses are faced with burgeoning compliance costs. They face an unclear business environment with no way of estimating where and when they will be taxed. Business expansion is chilled, especially when it comes to electronic commerce which inherently crosses state borders. And companies face the risk of duplicative taxation, since they also face legitimate taxes from the states in which they are domiciled.

Atlantic Technology, a small business based in Norwood MA, is a typical example. A true model of American ingenuity, Atlantic Technology was founded in 1989 by Peter Tribeman and produces a variety of home entertainment products, including high-performance multi-channel speaker systems and state-of-the-art home theater electronics components. Although the company has no physical presence in the state of Washington, Washington’s Department of Revenue has continually taxed Atlantic Technology because of their use of independent sales representatives. While the company contested this assessment, they were faced with additional

tax levies by other states including Pennsylvania and Florida. Fighting this barrage of state taxes will require the use of scarce resources that should be going toward building the business.

Mitek, a family-owned and operated business, which is based in Phoenix, Arizona, is facing a similar fight. Mitek produces well-known mobile audio brands such as MTX Audio and StreetWires. Mitek has been hit with business activity taxes in several states, including California, Washington and Michigan, strictly based on the use of nonexclusive independent representatives.

For Atlantic Technology, Mitek and numerous other companies that are forced to pay taxes in states where their company has no physical presence; these taxes are negatively impacting innovation and the overall economy. The continued growth of the consumer electronics industry is due in part to the success of the Internet, which has created a national market for many small businesses. Unfortunately, the threat of being subject to out-of-state business taxes may lead some companies to cut ties and refuse serve customers.

It is imperative for Congress to step in and assume its constitutional responsibility to ensure that commerce is not harmed by unfair taxation. The Business Activity Tax Simplification Act, H.R. 5627 would provide the much needed relief to small businesses. We applaud the leadership of Representatives Rick Boucher (D-VA) and Bob Goodlatte (R-VA) in introducing this important legislation. H.R. 5627 will provide clarity by providing a bright line definition of physical presence. Most importantly, it provides relief to business by clearly preempting states from taxing corporations with no physical presence.

Let me be clear - our member companies are not asking for relief from legitimate taxation. We are asking to restore a simple principle: a tax should not be imposed by a state unless that state provides benefits or protections to the taxpayer. H.R. 5627 will not result in

reduction in taxes paid by businesses. Rather, the bill provides that only businesses receiving state and local benefits derived from such taxation like education, transportation, fire and police, should be subject to such taxes. Furthermore, the legislation will not impact states' ability to collect income or other legitimate taxes from its residents.

Congress has historically acted to invoke its Commerce Clause authority. For example, Congress enacted the Federal Aviation Act to prohibit states from imposing "flyover taxes," ensuring that aircrafts were only taxed by states where they take off and land. Recently, Congress enacted legislation to prohibit taxing Internet access and prohibit multiple or discriminatory taxes on electronic commerce. We urge Congress to act again to provide relief to small businesses that carry the heaviest burden when subjected to these predatory taxes.

As you know, small companies with fewer than 20 employees already spend significantly more per employee to comply with federal regulations, including tax compliance when compared to larger businesses. With this in mind, we need to protect small business from inappropriate taxation. This legislation will provide relief and greater clarity for small businesses, which are the lifeblood of the U.S. economy. Therefore, I respectfully urge you to say no to taxation without representation and support the Business Activity Tax Simplification Act (BATSA).